



ARIZONA STATE RETIREMENT SYSTEM

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*Paul Matson
Director*

MINUTES PUBLIC MEETING ARIZONA STATE RETIREMENT SYSTEM BOARD

**Friday, November 19, 2010
8:30 A.M., MST**

The Arizona State Retirement System (ASRS) Board met in the 10th Floor Board Room, 3300 N. Central Avenue, Phoenix, Arizona. Mr. David Byers, Chair of the ASRS Board, called the meeting to order at 8:31 A.M., MST.

The meeting was teleconferenced to the ASRS office at 7660 E. Broadway, Tucson, Arizona 85710.

1. Call to Order; Roll Call; Opening Remarks

Present: Mr. David Byers, Chair
Mr. Tom Connelly, Vice-chair
Mr. Chris Harris (via telephone)
Professor Dennis Hoffman (arrived at 8:32 A.M.)
Mr. Tom Manos
Mr. Michael Townsend
Mr. Larry Trachtenberg (via teleconference)
Mr. Steve Zeman

Absent: Mr. Kevin McCarthy

A quorum was present for the purpose of conducting business.

2. Approval of the Minutes of the September 29, 2010 Public Meeting and Executive Session of the ASRS Board and October 15, 2010 Public Meeting of the ASRS Board

Professor Dennis Hoffman arrived.

Motion: Mr. Chris Harris moved to approve the minutes of the September 29, 2010 Public Meeting and Executive Session of the ASRS Board and October 15, 2010 Public Meeting of the ASRS Board. Mr. Steve Zeman seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

3. Presentation, Discussion and Appropriate Action Regarding Investment General Consultant Contracts and Other Board Approved Contracts

Mr. Paul Matson, Director, addressed the Board regarding general investment consultant contract renewals and other Board approved contracts. He noted in the past, the standard operating procedure has been to automatically renew general investment consultant, actuarial, and financial audit contracts unless the Board indicated otherwise. Upon further review of the Governance Handbook, it appears that the most reasonable interpretation is that the Board formally approve the contract renewals. Mr. Matson explained these contract renewals are past due as a result of a staff oversight. Mr. Matson said the staff recommendation is that the Board approve the renewal of the

existing general investment consulting contracts.

Motion: Mr. Tom Connelly moved to approve the renewal of the investment general consultant contracts for Callan Associates, Meketa Investment Group, Inc., Mercer Investment Consulting, NEPC, and Strategic Investment Solutions (SIS). Mr. Chris Harris seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

4. Presentation, Discussion and Appropriate Action Regarding the 2011 Legislative Session

Ms. Lesli Sorensen, Government Relations Officer, addressed the Board regarding the 2011 Legislative elections, giving an update on who was elected.

5. Presentation, Discussion and Appropriate Action Regarding the Global Tactical Asset Allocation (GTAA) Program Review

Mr. Gary Dokes, Chief Investment Officer, and Mr. Mike Lewis, Principal, Alternative Investment Research, Mercer, addressed the Board regarding the ASRS GTAA program, which began in January 2004, and provides for the tactical investment between asset classes. Such tactical, active decisions are anticipated to provide incremental return relative to the ASRS Total Fund Benchmark. As of September 30, 2010, the total market value of the ASRS GTAA asset class was \$2.6 billion, or approximately 10.3% of the Total Fund. The GTAA asset class policy target/range is 10% \pm 2%.

6. Presentation, Discussion and Appropriate Action Regarding Proposed Modifications to the ASRS Long Term Disability (LTD) Program

Mr. Gary Dokes and Mr. Eric Glass, Portfolio Analyst, addressed the Board regarding modifications to ASRS LTD Strategic Asset Allocation (SAA) and modifications to the ASRS Strategic Investment Policy #004 regarding the rebalancing of ASRS LTD Program assets. Modifications would improve program cash-flow liquidity and rebalancing flexibility, would reduce fees and improve anticipated fund performance, and would provide better SAA policy alignment to the ASRS Plan asset allocation policy. The Investment Committee (IC) recommends the Board approve the proposed modifications.

Motion: Mr. Chris Harris moved to approve the modifications to the ASRS LTD Strategic Asset Allocation (SAA) as noted in red in Exhibit 1, and approve modifications to the ASRS Strategic Investment Policy #004 regarding the rebalancing of ASRS LTD Program assets as noted in Exhibit 2. Professor Dennis Hoffman seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

7. Presentation, Discussion and Appropriate Action Regarding the ASRS Long-Term Investment Rate of Return Assumption

Mr. Matson addressed the Board regarding the ASRS' 8% long-term investment rate of return assumption. Mr. Matson said a discussion of the 8% rate of return objective occurred at the September 2010 Board strategic planning session meeting. As a result, the IC met on November 3 to continue this discussion and specifically focus on the investment market and economic building blocks that determine reasonable estimates for expected long-term rates of return. Mr. Matson then discussed near-to-intermediate term investment market conditions and asset class performance expectations with a greater emphasis placed on long-term investment market expectations (20 to 30 years) and evaluating expected returns given ASRS' strategic asset allocation policy. Based upon the long-term nature of the investment rate of return assumption, 8% is a reasonable and prudent

assumption.

Mr. Matson explained the ASRS' 8% long-term investment rate of return assumption is used to determine ASRS aggregate fund liabilities, funded status, and the timing of subsequent contribution rates. Focusing on the long-term investment rate of return assumption is important given its significant effect on determining liabilities and the funding of pension liabilities over time.

Mr. Matson noted, in addition to the traditional economic analysis discussions of the most appropriate long term investment rate of return assumption, additional factors that support the reasonableness of 8% as the long-term investment rate of return assumption include:

- The ASRS has a multi-generational time frame that incorporates both the current economic environment (non-normal) as well as future economic environments.
- The ASRS has salary inflation assumptions that are possibly higher than near-term expectations. This inflation expectation is likely correlated with, and would therefore likely result in an offset to, ex-post differences in long-term investment rate of return assumption.
- Ex-post differences from long-term investment rate of return assumption are captured annually in return experience differentials and are already incorporated into contribution rates on a smoothed ten-year basis.
- A change in ex-ante long-term investment rate of return assumption could be incorporated immediately or allocated over time. If allocated over time, the result would be similar to the return experience differential smoothing described above.
- Maintaining the current long-term investment rate of return assumption still allows for future reviews and possible modifications of the actuarial interest rate.
- The long-term trajectory of contribution rates would suggest that inter-generational equity in cost-sharing (paying of contribution rates) is perhaps best supported by considering contribution rate increases once contribution rates have begun their reversion to normal cost (a lower rate).

Discussion ensued regarding the possible effect on contribution rates if the rate of return were to be adjusted from 8% higher or lower. Mr. Trachtenberg said although it would not be appropriate to determine the long-term investment rate of return based upon its impact on contribution rates, the ASRS should also not be changing long-term views on rate of return based on short-term aspects of the economy.

Mr. Matson pointed out the IC and staff recommend the Board approve maintaining the current long-term investment rate of return of 8% and continue to review for long-term reasonableness in subsequent years. This would result in the 8% long-term investment rate of return continuing for periods beginning July 1, 2011.

Motion: Mr. Tom Connelly moved to approve the Investment Committee recommendation to the Board to maintain the current long-term investment rate of return assumption of 8% and continue to review for long-term reasonableness in subsequent years. Mr. Michael Townsend seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

8. Presentation, Discussion and Appropriate Action Regarding the Calendar Year 2011 Board Meeting Calendar

Mr. Dave Byers addressed the Board regarding the 2011 Board meeting calendar. Trustees discussed possible meeting dates in 2011. General consensus was to hold meetings on February 18, March 18, April 15, May 20, June 17, July 15, September 9, October 21, and November 18. All Board meetings will begin at 8:30 a.m.

Motion: Mr. Michael Townsend moved to approve the 2011 Board meeting schedule, with most meetings to be held on the third Friday of the month. Mr. Chris Harris seconded the motion.

It was noted the September meeting will be held on the second Friday of the month due to a furlough day.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

9. Director's Report

Mr. Matson presented the Director's Report. He noted members have provided positive comments regarding the Health Insurance Open Enrollment currently underway. They feel the brochure is easier to understand than in the past.

Mr. Matson said valuations will be presented at the December Board meeting. He is familiar with the data and is in the process of authorizing the same 13th checks for "System" members as last year. There will be no increase. The checks should be issued before Christmas.

Mr. Matson introduced Mr. Dave King, the new Member Services Division Assistant Director.

Mr. Matson explained the Board Governance Handbook calls for fiduciary education to occur annually. However, because five trustees are potentially up for reappointment, he would like to maximize the value of the training and wait until next Spring.

10. Presentation and Discussion with Respect to Informational Updates from the Operations Committee, Investment Committee, and External Affairs Committee

Mr. Michael Townsend, Chair, External Affairs Committee, said the next External Affairs Committee meeting will take place December 3, 2010.

Mr. Tom Connelly, Chair, Investment Committee (IC), said the next IC meeting will take place December 13, 2010.

Mr. Steve Zeman, Chair, Operations Committee (OC), said the next OC meeting will take place December 9, 2010.

11. New Agenda Items

No requests were made.

12. Call to the Public

No members of the public requested to speak.

13. The next ASRS Board meeting is scheduled for Friday, December 17, 2010, at 8:30 A.M., at 3300 N. Central Avenue, 10th Floor Board room, Phoenix, Arizona.

14. Adjournment of the ASRS Board

Mr. Byers adjourned the Board meeting at 10:23 A.M.

ARIZONA STATE RETIREMENT SYSTEM

Lisa Hanneman

Date

Paul Matson

Date

Board Secretary

Director